centreforcities

Agenda for Growth: September 2010

Firm Intentions:
Cities, Private Sector Jobs & the Coalition

Paul Swinney, Kieran Larkin & Chris Webber

Executive Summary

The new Government wants to increase private sector jobs growth, rebalance the economy and decentralise power to local communities. It will soon release a White Paper on sub-national growth explaining how it intends to achieve these objectives, but it is already clear that it faces an uphill struggle. Most importantly, the huge spending constraints the public sector now faces mean that, in order to achieve their growth objectives, public sector actors will need to adopt policies that are both more realistic and more effective than they have been in the past. This paper builds on our recent *Private Sector Cities* report to provide local and national decision makers with advice on how they can do this.

In section one, it highlights some **key lessons on the nature of private sector growth in England** and calls for a more pragmatic attitude towards business growth policy from all tiers of government. The scope of sector support policies, for example, is out of control. Almost 70 percent of England's cities now identify the creative industries as one of their priority sectors, even though in many of these places the scale of the industry is small and growth has been minimal.

Government does have a role to play in directly supporting business growth, but it needs to be smarter about how it approaches this challenge and focus scarce resources where they can have maximum impact. Paying closer attention to the six percent of 'high growth' businesses that accounted for over 50 percent of total jobs growth between 2005 and 2008 may be a more appropriate place to start.

In section two, the report looks at how **local enterprise partnerships can be used to maximise economic growth across the country**. These new partnerships will be the key vehicle for delivering private sector jobs in cities over the coming years. In order to do this, they need more powers from central government – over transport, for example – and that they need to have their own dedicated, un-ringfenced funding.

With support from

KPMG

City partners

Lancashire County Council

Preston City Council

The primary focus of local enterprise partnerships should be getting the basics right by strengthening skills and the general business environment in their areas – for example, by improving transport, housing and other infrastructure. They should also be thinking about how they can pool scarce resources and coordinate decisions across the partnership area, particularly over planning.

In section three, the paper explains **how the Government's new Regional Growth Fund can be used most effectively to maximise economic growth and create jobs.** Expectations about what this fund can achieve need to be kept in check because the size of the pot – £1 billion split over two years – is small in comparison to recent spending in this area.

"Money needs to be focused where it can have maximum impact on private sector growth"

The fund needs to have two main objectives: maximising private sector jobs growth in those areas where it can be sustained and supporting transition in those areas – such as Barnsley and Middlesbrough – still struggling with the challenges of long term industrial change. Maximising private sector growth should be the fund's key goal. For that reason, it should be focused on those cities able to make the strongest case for investment, including buoyant cities such as Brighton, Cambridge and Reading.

The emphasis on using the fund to support sustainable job creation in those cities most at risk of public sector job cuts should be dropped because using this criterion would not be the most effective way of targeting spending on sustainable jobs growth.

Acknowledgements

We are grateful to KPMG in the UK for their generous support and assistance in developing this document, and for their insights on city funding, financing and local economically driven decision making. We are also grateful to our local authority partners, Preston City Council and Lancashire County Council.

We are also indebted to a wide range of researchers and policy experts who helped to develop the thinking for this report and commented on earlier versions of it. Particular thanks are due to Max Nathan, Henry Overman, Bridget Rosewell and Commission for the New Economy Manchester.

Special thanks are also due to Alasdair Rae of the University of Sheffield for developing some of the maps used in the paper, and to Karen Bonner and Mark Hart of Aston University for producing city statistics on high growth firms.

As always, any errors are the authors' own and the views expressed within our independent report do not necessarily reflect those of our sponsors.

Introduction

The new Government wants to increase private sector jobs growth, rebalance the economy and decentralise power to local communities. But it is trying to achieve these goals against the backdrop of reduced public spending, and this implies big changes in the way that economic development policies are carried out. Since coming to power in May, the coalition Government has rapidly reshaped the landscape of economic development in England. Regional Development Agencies (RDAs) have been abolished and in their place local enterprise partnerships will be created, supported by the Regional Growth Fund. This paper will set out how these new tools for economic development should contribute to the Government's key goals.

"The scale of the task that policy makers face should not be underestimated"

The scale of the task that policy makers face should not be underestimated. By 2015/16, the Government expects to have made £99 billion per year worth of public spending cuts, almost two thirds of which were planned by the previous government. That is the equivalent of cutting spending per year by more than the UK currently spends on the entire education system (£88 billion in 2009/10) and it will be the most significant expenditure cut since World War II.

Some of these savings will be made through job cuts. The Office of Budget Responsibility (OBR) expects there to be 600,000 fewer jobs in the public sector by 2015/16. Our research has already shown that some cities, such as Hastings and Newcastle, are more vulnerable than others to the coming cuts.[1]

October's Comprehensive Spending Review (CSR) will give us the detail on how these cuts will impact on the budgets of local authorities and Whitehall departments. Cities should be under no illusions about the vulnerability of their own budgets or of central government spending in areas like regeneration and transport. In the Budget, the Government projected that the spending of unprotected departments will be cut by 25 percent by 2014/15, and has asked departments to prepare plans for cuts of up to 40 percent.[2]

In parallel to taking action to reduce the deficit, the Prime Minister and his Deputy have been talking about their desire to rebalance the economy. There are four main strands to their vision: rebalancing from the public sector towards the private sector; from domestic consumption to exports; from finance towards manufacturing; and from London and the South towards the North and Midlands.

But rebalancing will be a difficult task. For example, as the Centre for Cities showed in June, the weak private sector performance during the economic boom of many cities in the North and Midlands – including places like Birmingham, Stoke and Blackpool – means that a significant rebalancing of private sector activity towards these areas during recovery from recession is unlikely to occur. In section one of this report we highlight four lessons about private sector jobs growth in England that suggest the new Government should be more realistic in its approach to rebalancing.

---

1. Larkin K (2009) Public Sector Cities: Trouble ahead, London: Centre for Cities
2. HM Treasury (2010) Budget 2010, London: HM Treasury; Guardian (2010) 'Treasury orders cabinet ministers to brace themselves for 40% cuts', published in The Guardian, 3 July 2010

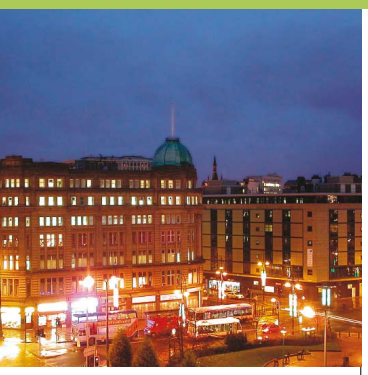
Section two focuses on how private sector jobs growth might be delivered. Both local and national government still have an important role to play in driving up private sector growth. Over the coming years the key institutional vehicles for delivering private sector growth at a local level will be local enterprise partnerships. The idea is that these will be partnerships between groups of local authorities and businesses that will 'provide the strategic leadership in their areas to set out local economic priorities'.[3]

Local enterprise partnerships are a good idea because they offer the chance of devolving decision-making to real economic areas. However, they are at risk of being a wasted opportunity because the debate about them is currently far too focused on what geographical areas they should cover rather than what they should actually do to drive forward economic growth.[4] In section two of this paper, we try and open up a more useful discussion on what partnerships should do to support private sector growth by setting out which areas of policy partnerships should have responsibility for and what they should do with their powers.

"The majority of the fund's spending needs to be focused on those areas most capable of generating private sector jobs"

In the short term, local enterprise partnerships will be accompanied by the Regional Growth Fund. This is a £1 billion fund that will be split over two years. The final section of this report argues that the Regional Growth Fund's suggested goals need to change. The majority of the fund's spending needs to be focused on those areas most capable of generating private sector jobs. Support for struggling cities should not be assessed against the objective of creating new private sector activity.

3. Cable V & Pickles E (2010) Local enterprise partnerships, letter to local authorities, 29 June 2010
4. The areas that the partnerships cover is important, but it is only one part of a much more important discussion of what they should actually do.



1. Four lessons on private sector jobs growth in England and what they mean for policy

'Rebalancing' has become one of the new Government's key terms. In his first speech as Prime Minister, David Cameron said that we need to 'rebalance economic power across our regions'.[5] Nick Clegg wants to 'foster a thriving and more balanced economy so that no region or community gets left behind'.[6] And Vince Cable has talked about 'an economy that is highly unbalanced both in its sectors and its regions'.[7]

The idea of rebalancing might play well with voters, but it does not take account of some important truths about the way our economy operates and could easily lead to policies that are ineffective at creating jobs. This section of the report picks out four realities about private sector growth in England and sets out the policy implications for national and local government.

"The idea of rebalancing might play well with voters, but it ignores some important truths about the way our economy operates"

- **Private sector growth is uneven across England's cities** and government does not have the power to smooth it out.
- **Manufacturing will not be a major source of future private sector jobs growth** so government should manage expectations about a manufacturing renaissance.
- **Not everywhere can have a powerful creative, advanced manufacturing or green industries cluster** so cities should be more realistic about their aspirations for future jobs growth in these areas.
- **Most new private sector jobs come from a small number of firms** so government should consider increasing its focus on these 'high growth firms' if it wants to maximise private sector growth.

Private sector growth is uneven

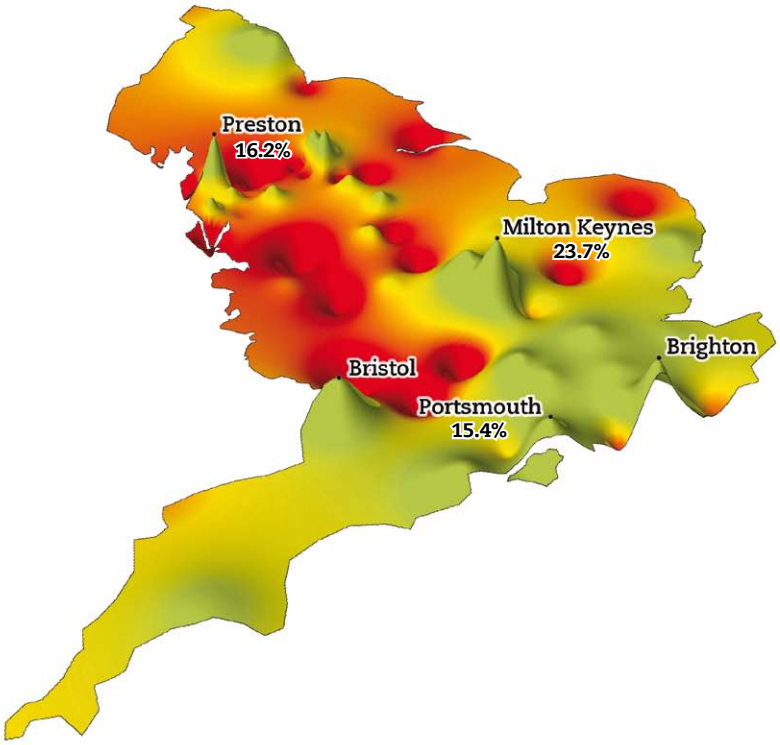
As shown in our *Private Sector Cities* report earlier this year, private sector performance varies significantly across England and government has little direct control over where private sector jobs are likely to be created. Instead of continually attempting to redraw the pattern of private sector growth, therefore, policy makers seeking to encourage jobs growth should focus more of their efforts on physically expanding those areas – such as London, Reading and Brighton – that are experiencing the highest levels of private sector growth.

Differences between cities in recent private sector performance have been stark. Between 1998 and 2008, Brighton and Milton Keynes both grew their private sector jobs bases by 25 percent. Wakefield and Preston increased theirs by 13 percent and 16 percent respectively over the same period. At the other end of the spectrum, some of the weakest performers were places like Stoke (-16 percent), Blackburn (-12 percent) and Blackpool (-6 percent).

---

5. Speech delivered by David Cameron, 28 May 2010, Transforming the British economy: Coalition strategy for economic growth
6. Nick Clegg launches £1 Billion fund to help regional business, Press release, 29 June 2010
7. Cable presses banks on business loans, Financial Times, 3 June 2010

Figure 1: Percentage private sector growth across England (1998-2008)[8]



***Source**: NOMIS 2010, Annual Business Inquiry, workplace analysis. Estimates based on jobs added between 1998-2005 and 2006-2008 to take into account changes in ABI methodology.*

"Successive governments have tried hard to counteract these kinds of disparities in economic performance, but with little success"

Successive governments have tried hard to counteract these kinds of disparities in economic performance, but with little success. Labour's Regional Economic Performance Public Service Agreement aimed to reduce the gap in growth rates between regions, but failed to do so. The current Government's one year National Insurance holiday for the first ten employees of new businesses started in the North, Midlands and South West is the latest example of such a policy with similar aims.

The main reason regional policies have consistently failed to live up to expectations is that government actors have been working against powerful long-term trends like globalisation and technological change, which have been gradually redrawing the natural geography of private sector growth in England. No reasonable amount of government investment could counteract the shift because the economic impact of these forces dwarfs the spending power of government.

Although understandable, the current Government's wish to rebalance the distribution of economic activity in England will prove difficult to turn into reality because it runs counter to the way our economy operates. People must be able to access jobs, but decision makers should accept that they have little direct control over where these jobs are going to be located. If the objective is to support the creation of as many sustainable jobs as possible, the clear implication is that more policy effort should be focused on expanding those areas experiencing growth so that people from all over the country can access the opportunities being generated.

8. Our public-private split will exclude some private sector activity classified under education and health. See Larkin K (2009) Public sector cities: Supporting paper, London: Centre for Cities for a discussion of our definition of the public and private sector and the associated issues of data availability at city level.

This conclusion does not mean that struggling cities – such as Middlesbrough and Blackburn – should receive no public attention; quite the contrary. Valuable economic activity occurs in these places and many thousands of people are employed in them. The fact remains, however, that even during a period of strong national growth, many of these cities were losing private sector jobs, so it seems unlikely that they will be major centres for private sector jobs growth over the next decade. A new approach is needed to economic development in these cities, and the third paper in our *Agenda for Growth* series will be looking at this issue in detail.

Policy implications

- **Policies that aim to boost private sector jobs growth are best targeted at cities that have strong private sector economies and have a good record of private sector job creation.**

- **Struggling cities are unlikely to be able to support sustainable private sector jobs growth, and so a new approach to economic development is required in these cities.**

"Policies that aim to boost private sector jobs growth are best targeted at cities that have strong private sector economies"

Manufacturing will not be a major source of future private sector jobs growth

Politicians highlight the need for a manufacturing renaissance that can help rebalance the economy and provide more private sector jobs.[9] The political rationale for such rhetoric is clear, but this is detached from the economic reality. England needs new private sector jobs, but the manufacturing sector will not be a primary source of them.

Manufacturing is an important industry for our economy. The UK remains the sixth largest manufacturing nation in the world by the value of goods it produces, and England accounts for 83 percent of this output.[10] However, British manufacturing has had to rely on productivity improvements to remain competitive. As a result the proportion of the workforce employed in the sector has declined steadily for decades.

As Figure 2 shows, the decline of manufacturing employment has been one of the clearest trends characterising the UK's economic evolution over the past 40 years. Between 1970 and 2007, the share of the UK's workers employed in manufacturing dropped from 32 percent to 11 percent. This trend is not unique to the UK. Even in Germany, a country with a much stronger modern manufacturing reputation than the UK, the same competitive pressures have driven a considerable decline in employment in the sector since the 1970s.

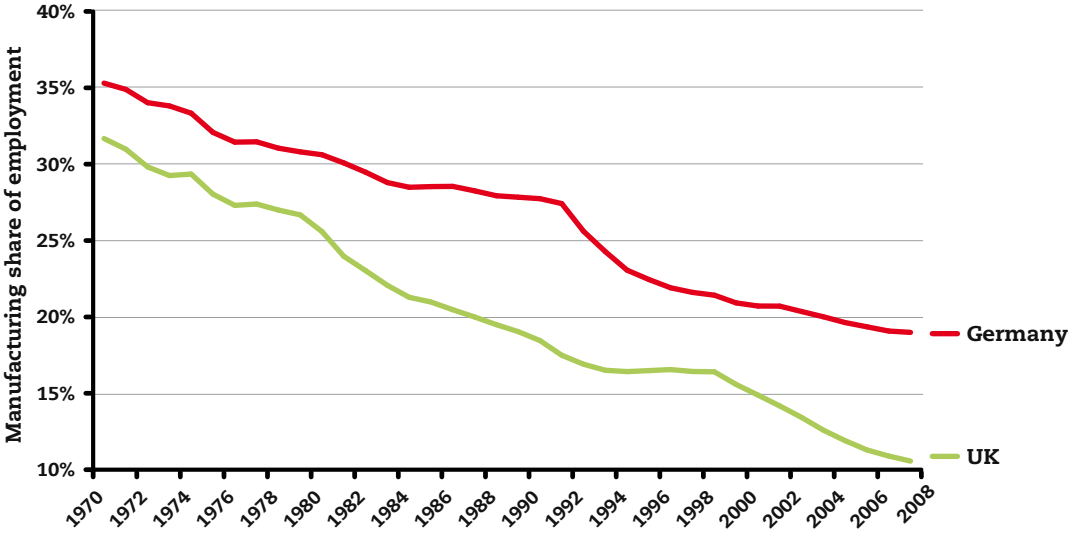
The decline in manufacturing employment has hit many of England's cities hard. Between 1998 and 2008, every one of England's 56 cities experienced a drop in total manufacturing employment. The average net fall was 33 percent.[11] In Stoke it fell by 57 percent (27,800 jobs). In Leicester it fell by 45 percent (24,000 jobs).

---

9. Speech delivered by David Cameron, 28 May 2010, Transforming the British economy: Coalition strategy for economic growth
10. ONS (2010) 2007 data
11. NOMIS 2010, Annual Business Inquiry, workplace analysis. Estimates are based on jobs added between 1998-2005 and 2006-2008 to take into account changes in ABI methodology.

"The UK does not have the same specialism in goods production as countries like Korea and Germany"

Figure 2: Manufacturing share of employment in the UK and Germany (1970-2007)



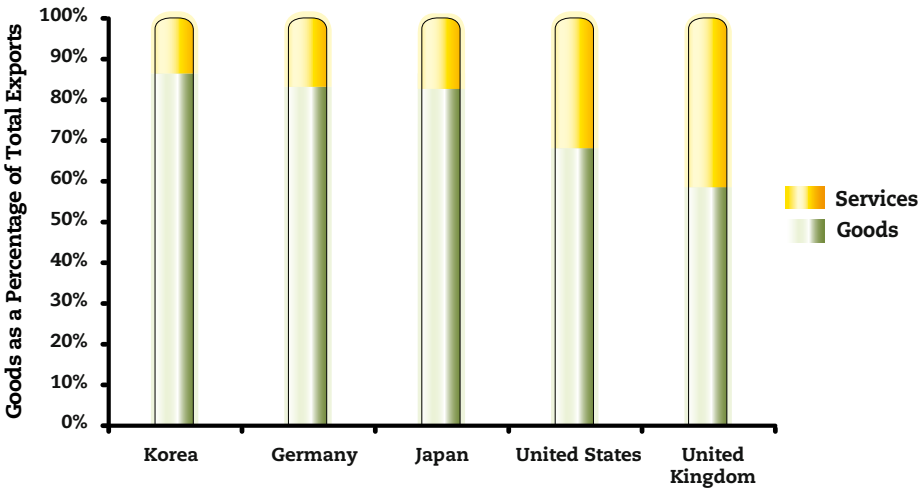
Source: *EU KLEMS (2010)*

Of course, some manufacturing firms did create jobs over this period. And some firms will continue to do so in the future, aided by the more favourable exchange rate. These firms are likely to be located in higher value activities where the total job creation may not be very large. As such, this is unlikely to be enough to halt the continued overall decline in employment in the sector.

The UK does have a niche in some areas of manufacturing, such as engineering and pharmaceuticals.[12] However, in these higher value activities the boundaries between manufacturing and services are becoming increasingly blurred. An increasing share of Rolls Royce's revenues, for example, comes from aftercare services.

As Figure 3 shows, despite advantages in key industries, the UK does not have the same specialism in goods production as countries like Korea and Germany.[13]

Figure 3: Export of goods as a percentage of total exports (2009)



Source: *OECD (2010)*

12. Leunig T & Tennant K (2010) Decline and fall: A history of UK post-war textile production, London: Department for Business, Industry & Skills
13. More specifically, the UK does not have a comparative advantage in goods production. At an aggregate level it is better for the UK to acquire goods through trade rather than producing them itself.

The yellow bars of the chart show the corresponding comparative advantage in services. For example, 41.5 percent of the UK's exports were services, compared to just 16.8 percent of German exports. Given this key strength, most net future employment growth is likely to continue to come from the services sector, as it has done over the past 30 years.[14]

Policy makers need to be more realistic about the potential for future net employment growth in the manufacturing sector. Prioritising policy and scarce government resources on the idea of a manufacturing renaissance is unlikely to lead to a positive outcome in terms of private sector jobs growth.

Policy implication

- **Government should not seek to promote manufacturing as a major source of private sector jobs growth.**

"Government should not seek to promote manufacturing as a major source of private sector jobs growth"

Not every city can have a powerful creative, advanced manufacturing or green industries cluster

Policy makers know that England's economy is changing, and they can be found promoting the prospects of the latest key business sector.[15] It is crucial that policy makers understand their economies, and analysing the development needs of individual sectors is an important way of doing this. But the focus on priority sectors and bringing forward policies to support them has led to some hugely unrealistic strategies and interventions in England's cities. Going forward, both local and national policy makers need to adopt a much more pragmatic approach to the idea of sector policies, and in many cases should consider dropping them altogether.

The extremes to which sector policies have been adopted becomes clear when you review how many different cities around England have prioritised sectors like creative industries and advanced manufacturing. **Our research shows that 39 of 56 cities in England believe they have a creative industries sector worth supporting or developing, 26 are shooting for a green industries sector and 33 identify advanced manufacturing as a current or future key strength. Fifteen of these cities are aiming for all three.**

Using broad sector definitions that have some degree of overlap,[16] Figure 4 shows the top five sites for employment in England of four common priority sectors – creative industries, life sciences, advanced manufacturing and green industries. Cambridge, Aldershot[17] and Reading appear in the top five employment share for each of the four industries. But even given the liberal definitions and overlap between sectors, in most cities not very many people are employed in these sectors. For example, only around six percent of employment in Aldershot is in the life sciences sector – that's only 4,400 jobs. And that is for a city where employment in this sector is abundant.

---

14. Manyika J (2010) How to compete and grow: A sector guide to policy, San Francisco: McKinsey Global Institute
15. Speech delivered by David Cameron, 28 May 2010, Transforming the British economy: Coalition strategy for economic growth; Speech delivered by Nick Clegg, 11 February 2010, Liberal Democrats launch green jobs manifesto pledge
16. There are cases where the lowest level of Standard Industrial Code could easily be defined in more than one of our sectors. The most common one is "Research and experimental development on natural sciences and engineering", which we include in biosciences and research, advanced manufacturing and green technologies. Although further research could break down the SIC code further, the point here is that even with a more liberal definition, not many people are employed in these sectors.
17. Aldershot PUA encompasses Rushmoor and Surrey Heath.

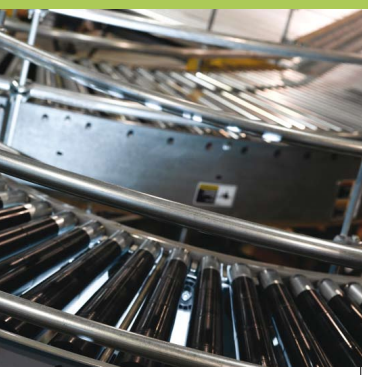
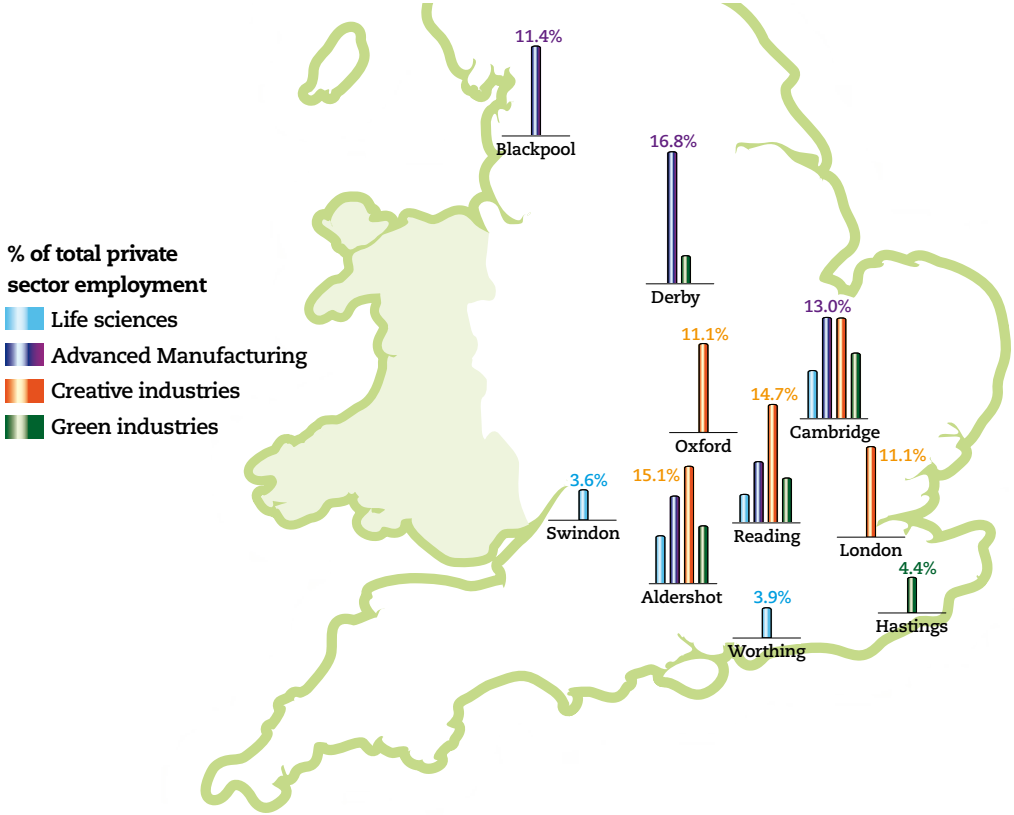


Figure 4: Top five sites of employment in four 'key' sectors (2008)[18]



Source: *NOMIS (2010) Annual Business Inquiry, workplace analysis*

"The Government's ability to stimulate the growth of new business clusters is limited"

Some will argue that government should be stepping in to try and encourage the growth of these kinds of industries where they have not yet taken root. Where this builds on assets its worth considering, but all too often this kind of thinking is based more on hope than reality.

First, as a matter of definition not every city can have a specialist life sciences sector. Second, given that clusters are likely to emerge as the result of some natural or historical advantage, such as a particular mix of local assets, it is unlikely that all cities would be equally well placed to develop such specialisms.

Third, the Government's ability to stimulate the growth of new business clusters is limited. For example, one international study found that 'other', including government intervention and random events, was cited as the most important determinant of a cluster's success in just 3.7 percent of studies of the world's ten most competitive clusters in their industry. The study also found that clusters where government had been the key determinant were found to be the least competitive.[19] Work by McKinsey has highlighted the high cost incurred by governments around the world who have tried to establish local semiconductor clusters, the majority of which have failed to achieve a sustainable competitive advantage.[20]

---

18. Our sectors are based on commonly used SIC code definitions. They are Eurostat (advanced manufacturing and engineering), Yorkshire Forward (life sciences), Department for Culture, Media and Sport (creative industries) and DTZ (environmental). A full description of the sector definitions and the underlying data is available at www.centreforcities.org/firmintentions
19. Van der Linde C (2003) 'The demography of clusters – findings from the cluster meta-survey' in Brocker J, Dohse D & Soltwedel R (eds.) Innovation clusters and interregional competition, New York: Springer-Verland
20. Manyika J (2010) How to compete and grow: A sector guide to policy, San Francisco: McKinsey Global Institute

Public sector actors clearly need to be more realistic about the growth potential of different business sectors around the country and their role in directly supporting the emergence of new industries. But being more realistic about the approach to different sectors does not mean ignoring them.

Public sector actors should always make an effort to understand the development needs of their business community and particular sectors within it. There may also still be a case for tailoring some existing policies, such as skills or property development, so that they reflect the needs of existing sectors.[21] However, a higher standard of justification should be applied to these types of intervention than has generally been the case in the past.

Policy implications

- **In general, local authorities should not seek to support 'key' sectors with specific policies.**
- **In some cities that are dominated by a large employer or certain sector, some policies may need to be tailored to an industry specific issue.**

"Research shows that a relatively small number of high growth firms are where most new jobs tend to come from"

Most new private sector jobs come from a relatively small number of high growth firms

A better way to understand the dynamics of private sector growth in the economy is to think about the performance of actual firms. Research shows that a relatively small number of high growth firms[22] are where most new jobs tend to come from. These firms are visible right across the industrial spectrum, rather than being located in any one particular sector. Instead of getting preoccupied with different types of sector intervention, government actors might be able to have a bigger impact on private sector job creation if they can enable the growth of these businesses.

Work sponsored by NESTA[23] in 2009 found that just six percent of firms accounted for over half of the employment growth of all 'survivor'[24] firms between 2005 and 2008. Subsequent data commissioned by the Centre for Cities[25] shows that 64 percent of high growth firms are headquartered in cities. However, the distribution of high growth firms around the country is highly uneven. In terms of absolute numbers, high growth firms are highly skewed towards London (Figures 5b & c). A different picture emerges when looking at the percentage of high growth firms of all 'survivor' firms. Aldershot has the highest share (8.5 percent) and Worthing (2.8 percent) the lowest (see Figure 5a).[26]

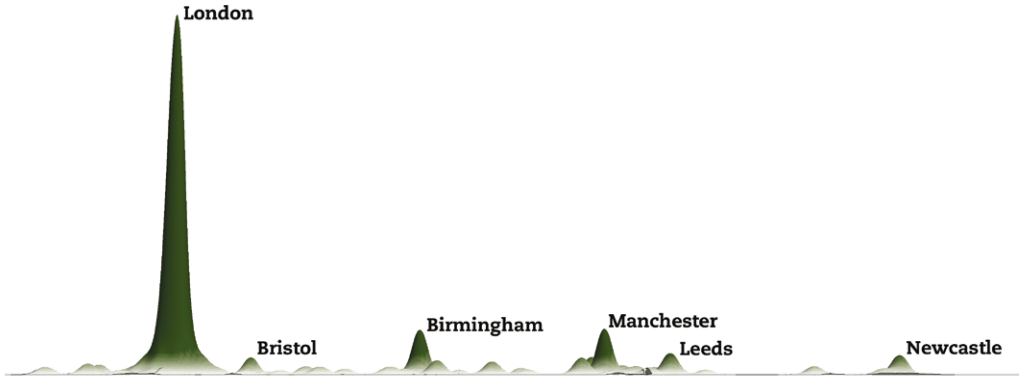
---

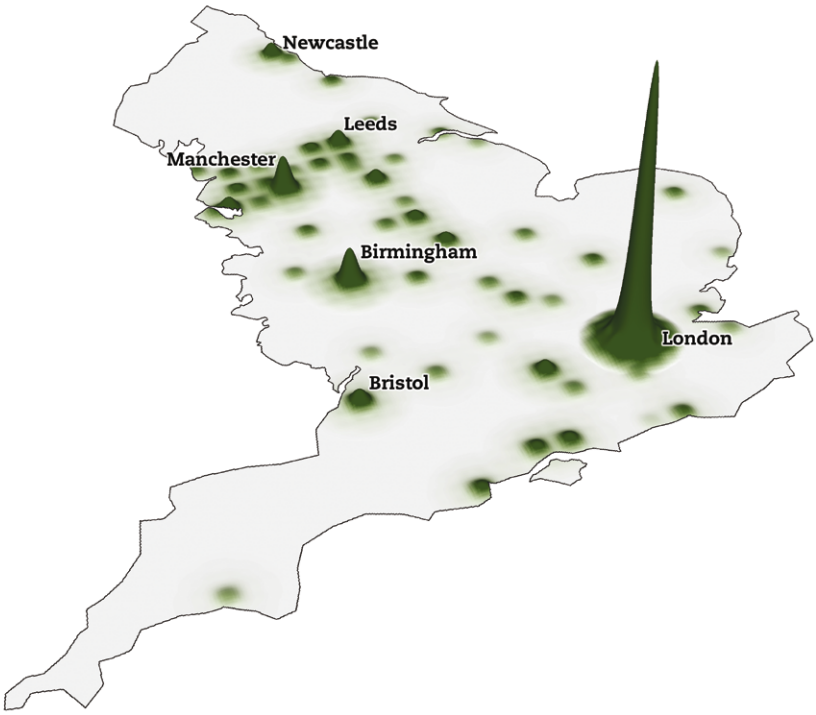
21. Knell J & Oakley K (2007) London's Creative Economy: An Accidental Success?, London: The Work Foundation
22. These are defined as those businesses larger than ten employees that achieve an average annual growth rate in their number of employees of 20 percent or above over a three year period. This definition does not distinguish between internal 'organic' job creation and expansion through an acquisition of another firm, and currently there is no reliable way to do this on the IDBR.
23. Anyadike-Danes M, Bonner K, Hart M & Mason C (2009) Measuring Business Growth, London: NESTA
24. A business which had non-zero employment for each of the years in the analysis and which were not 'born' (i.e. employed their first employee using the definition of a '1' employer enterprise) in the first year of each period.
25. The analysis of HGF data using the BSD was undertaken by Karen Bonner and Mark Hart (Economics and Strategy Group, Aston Business School, Aston University).
26. Firms were identified using the postcodes of their headquarters. In cases where a postcode sector could be attributed to more than one local authority, it was allocated to the local authority with the greatest number of wards in that postcode sector.

Figure 5a: Distribution of high growth firms across England's cities (2005-08)

Rank	City	% of firms that are high growth	Rank	City	% of firms that are high growth
1	Aldershot	8.5	47	Stoke	4.7
2	Wigan	7.8	48	Huddersfield	4.6
3	Telford	7.6	49	Sheffield	4.6
4	Reading	7.1	50	Leicester	4.5
5	Cambridge	7.1	51	Rochdale	4.5
6	Swindon	7.0	52	Chatham	4.4
7	London	6.9	53	Birmingham	4.3
8	Crawley	6.8	54	Bolton	4.1
9	Warrington	6.5	55	Burnley	3.9
10	Newcastle	6.5	56	Worthing	2.8*

Figure 5b & c: Profile and map of absolute number of high growth firms across England's cities (2005-08)



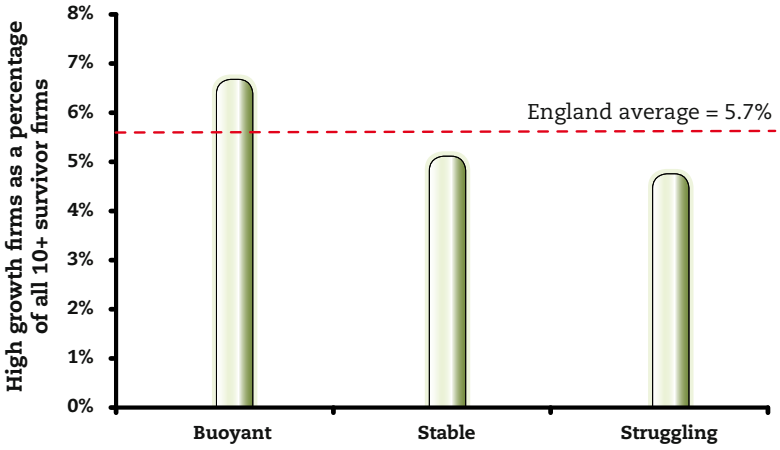


Source: *ONS: Business Structure Database (BSD)*
**This is an upper bound estimate, assuming that Worthing has nine high growth firms. As part of the data licence, users of the BSD are not allowed to disclose figures that are less than 10 and so this number is included for illustration only.*

"Focusing more of their efforts on high growth firms could help local and national government maximise their impact on private sector jobs growth"

In the first paper in this research series[27] we classified England's cities as either buoyant, stable or struggling based on their performance across a series of metrics. Looking at these categories using the high growth firms data, it is clear that buoyant cities have the most high growth firms relative to their overall stock of 'survivor' firms. Struggling cities have the least; though they do not lag stable cities by far (see Figure 6).

Figure 6: Distribution of high growth firms (2005-08)



Source: *ONS: Business Structure Database (BSD)*

"There is a risk that high growth firm related interventions could end up being ineffective and wasteful"

Focusing more of their efforts on high growth firms could help local and national government maximise their impact on private sector jobs growth. Some business support policies do already try to target high growth firms, such as the North West Development Agency's £10m 'High Growth Programme'. These types of programmes have not been around for long so judging their effectiveness at this point is difficult. As with other forms of business support, any high growth project should be carefully evaluated to judge its usefulness.

The big problem that programmes aiming to support high growth firms will face is identifying high growth businesses and supporting them in an effective way. Only 38 percent of high growth firms experience more than one year of high growth and only 13 percent experience more than two years of high growth.[28] Also, a large academic literature on firm growth suggests that growth is essentially random with regard to firm size, financial performance and productivity.[29]

Getting around these kinds of challenges will be difficult, and there is a risk that high growth firm related interventions could end up being ineffective and wasteful. However, the fact that private sector employment growth is concentrated in such a small number of firms means that these firms are very important. The potential returns to identifying and supporting these businesses (or firms that could potentially become high growth) cannot be ignored. The next section discusses options for the support of high growth firms in more detail.

Policy implication

- **Policy makers should consider focusing their business support policies on high growth firms because this small number of firms have a large impact on overall job creation.**

27. Webber C & Swinney P (2010) Private sector cities: A new geography of opportunity, London: Centre for Cities
28. Anyadike-Danes M, Bonner K, Hart M & Mason C (2009) Measuring Business Growth, London: NESTA
29. Coad A (2007) Firm Growth: A Survey, Papers on Economics and Evolution 2007-03, Max Planck Institute of Economics

2. How can local enterprise partnerships help create private sector jobs?

From September 2010 onwards, local enterprise partnerships will begin to replace RDAs as the main lever for boosting private sector jobs growth in England's cities.[30] Public spending cuts mean that these new bodies will have to make better use of scarce resources to achieve this important jobs growth objective. The Centre for Cities supports the shift to local enterprise partnerships because the evidence suggests that matching city governance structures to functional economic areas can increase economic growth.[31] Issues remain about the composition of local enterprise partnerships, and we have explored these in a recent paper.[32] Here we explain what partnerships should do to encourage private sector growth. We make four key recommendations:

"The top priority for local enterprise partnerships must be to understand and improve the business environment using the wider drivers of growth"

The top priority for local enterprise partnerships must be to understand and improve the business environment using the wider drivers of growth.
Local authorities, RDAs and local economic development agencies have often been very concerned with direct business interventions, like sector support and inward investment. But at a time of constrained public funding, it is important to be realistic about what these types of interventions can achieve and focus on getting the basic conditions for growth right. Evidence shows that improving the business environment by focusing on housing, planning, skills and transport – *the wider drivers* – will probably have a far greater impact on the future of most cities' economies.

This will require the coordination and prioritisation of existing policy levers, but central government must also decentralise power.
Much of a local enterprise partnership's role should be about local authorities and businesses working together to coordinate and prioritise existing funding streams. However, in some areas, such as transport, central government will also need to grant partnerships new powers so that they can deliver better policy outcomes.

Local enterprise partnerships will need a dedicated source of un-ringfenced funding, with the government incentivising economic growth.
To really support economic growth, local enterprise partnerships must be more than just an institutional change. They should not just be smaller RDAs. In the medium term, the partnerships also need to have their own un-ringfenced source of funding so that they can best meet the needs of their economy.

Local enterprise partnerships have a role to play in directly supporting business growth, but need to be realistic and focused.
The partnerships' interventions will need to be underpinned by a high level of private sector engagement, with business expertise used to gain a better understanding of the local economy and to direct policy interventions. High growth firms should be a focus for the partnerships' activity because of their importance to employment growth. Partnerships dependent on a large employer or single sector need to think about their plans for managing a supply side shock that could impact significantly on local employment.

---

30. Cable V & Pickles E (2010) Local enterprise partnerships, letter to local authorities, 29 June 2010
31. Cheshire P & Magrini S (2005) European Urban Growth: throwing some economic light into the black box, LSE Working paper presented to European Regional Science Association Congress, Amsterdam
32. For a discussion of the other challenges faced by local enterprise partnerships see: Centre for Cities (2010) Beyond the Boundaries: Why cross-boundary collaboration matters and what this means for local enterprise partnerships, London: Centre for Cities

"Getting the basics right by focusing on the wider drivers of growth makes a city a better location for mobile firms and individuals"

The priority for local enterprise partnerships must be to understand and improve the business environment

The number one priority for a local enterprise partnership should be to understand and improve the business environment in its area by focusing on the wider drivers of growth. This is the main way that partnerships can have an impact on private sector jobs growth. This sub-section outlines why the wider drivers are so important to cities' economies.

The main policy levers that local enterprise partnerships have at their disposal to improve the business environment are **planning, housing, skills and transport – *the wider drivers***. Often local authorities have been overly concerned with more bespoke, direct business interventions, like sector policies, innovation and inward investment, before they have got the basics right. As outlined in Figure 7, local enterprise partnerships need to work through a series of steps to improve their business environment.

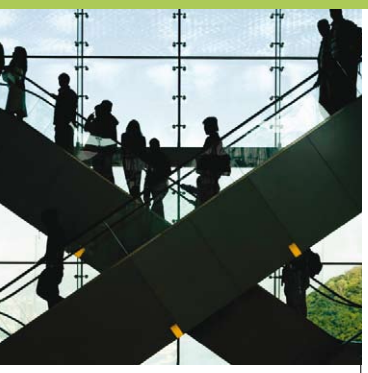
Figure 7: The steps local enterprise partnerships need to take to improve the business environment and encourage private sector jobs growth

Why are the wider drivers important?

Getting the basics right by focusing on the wider drivers of growth makes a city a better location for mobile firms and individuals, while at the same time improving individuals' opportunities. In particular, they reduce the costs faced by individuals and firms of locating and operating in a city.

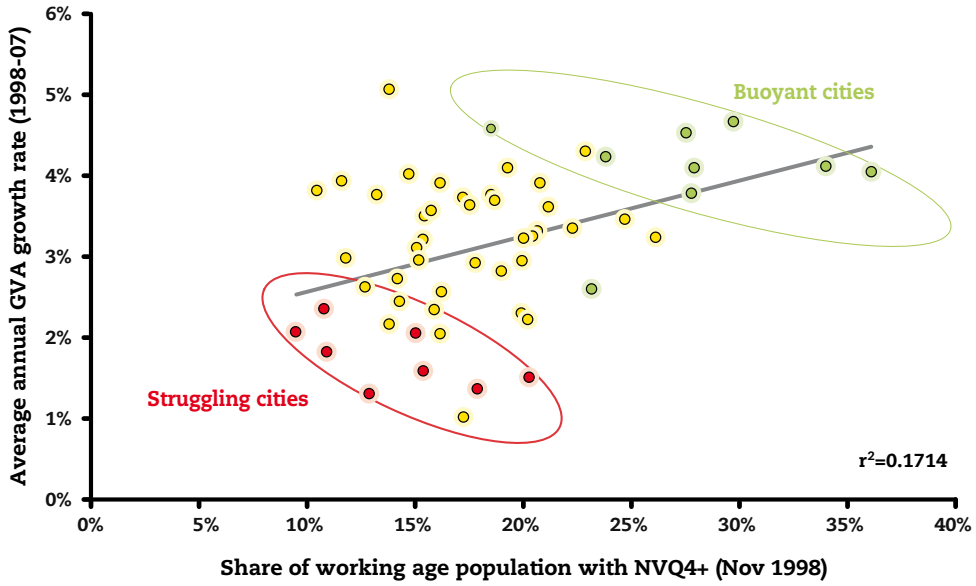
To understand why the wider drivers are important, it is worth considering what factors explain the relative performance of firms throughout the UK – why do some firms in certain places seem to do better? Research completed for the Manchester Independent Economic Review (MIER)[33] looked at which urban factors were associated with greater firm productivity (for a discussion of the relationship between productivity and jobs see Box 1).

33. MIER (2009) The Case for Agglomeration Economies, Manchester: AGMA



The research demonstrates that proximity to high economic mass e.g. being located in a city, access to lots of high skilled individuals and being close to key transport links – like motorways, ports and airports – explains much of the variation in the productivity performance of firms in the UK. Skills were found to be a particularly important factor – a relationship which can be demonstrated, albeit simplistically, by comparing a city's stock of high skilled workers in 1998 and its subsequent economic growth (Figure 8).[34]

Figure 8: Share of NVQ 4+ residents and subsequent economic growth (1998-2007)



Source: *NOMIS 2010, Labour Force Survey (Dec-Nov 1998 data); ONS, Regional Gross Value Added, own calculations*

"Evidence suggests that many place-based policies, like enterprise zones, are ineffective or excessively expensive"

Attempts to increase the density of certain sectors has been the explicit focus of many specialist industrial policies, but the MIER research found that, at an aggregate level, firms located in an area with lots of employment in the same sector were actually less productive overall, when controlling for the effects of economic density. Other work also supports the view that only firms in certain sectors are likely to benefit from being located close to other firms in the same industry and that the impact is likely to be less important than the benefit of just being located in a large urban area[35] with modern service sectors particularly likely to benefit from being located in a large city.[36] Equally, research suggests that many place based policies, like enterprise zones, are ineffective or excessively expensive.[37]

Instead, the evidence indicates that it is more important to focus on the wider drivers of economic growth than the concentration of specific sectors. In particular, the MIER research shows the importance of skills and more general economic density/city size, implying that the growth of Manchester should be supported.

34. While the correlation is fairly weak the clustering of struggling and buoyant cities suggests that this is an important relationship.
35. For example, one study found that firms in 13 out of the 27 broad sectors benefit from being located close to other companies in the same industry see: Graham D (2008) 'Identifying urbanisation and localisation externalities in manufacturing and service industries', Regional Science Vol 88(1): 63–84
36. Melo P, Graham D & Noland R (2009) 'A meta-analysis of estimates of urban agglomeration economies', Regional Science and Urban Economics Vol 39(3): 332-342
37. Glaeser E & Gottlieb J (2008) 'The Economics of Place-Making Policies', NBER Working Papers 14373

Box 1: Jobs or productivity growth?
Thinking about the wider drivers also raises the important distinction between the slightly differing objectives of jobs growth and productivity improvement. While it is natural for local policymakers to want to stimulate job creation, particularly given the current high level of unemployment, in the longer term productivity improvements are vital to increasing people's wages, wealth and prosperity and to supporting long term economic growth.

Although the wider drivers probably have a greater direct impact on productivity improvements, they should also generate new employment opportunities.

Coordination, prioritisation and devolution

"In order to improve the business environment three things need to happen: improved coordination, better prioritisation, and more devolution"

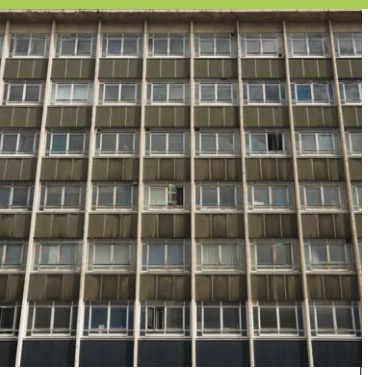
In order to improve the business environment three things need to happen: improved coordination, better prioritisation, and more devolution. In simple terms some powers need to be devolved down from the centre and others need to be 'devolved up' by local authorities. In this sub-section we set out what we mean by coordination, prioritisation and devolution and how they apply to the wider drivers of growth policy areas.

Many of the interventions that local enterprise partnerships need to make will require the coordination of powers that local authorities already have at their disposal – local authorities need to 'devolve power up'. In an era of fiscal constraint, co-ordinating policies across authority boundaries will take on an even greater importance. One way to co-ordinate policy is to set out strategic plans at the city-regional level, such as a spatial plan. Local authorities will need to make a judgement as to which policies will deliver better economic outcomes and be more cost effective when pooled and delivered by a partnership.

Prioritisation is particularly critical. This means choosing the interventions and investments that are in the best interests of a city region as a whole. For example, the local authorities in a partnership would benefit from pooling their local transport funding, with the partnership board then choosing between competing priority improvements or even spending the money on a non-transport related investment. This is more cost effective and likely to deliver better economic outcomes.

In order to make these difficult decisions and to improve the business environment, local enterprise partnerships need to develop a comprehensive understanding of the performance of their city economy against the wider drivers so that they can target underlying weaknesses. Robust economic analysis needs to underpin a partnership's decision making processes so that it can make the best investments and improve the returns achieved from public expenditure.

While partnerships already have some of the policy levers that they need within their control, further powers should be devolved to deliver better policy outcomes. Ministers have signalled that decentralisation is a top priority for the Coalition, a priority that we welcome.



We now outline what coordination, prioritisation and devolution look like in the context of the three wider drivers of economic growth – planning and housing, skills and transport.

Planning & housing

Enabling and encouraging physical development is one of the most obvious ways that cities can help to support economic growth in their area. A growing economy also needs sufficient houses, built in the right places and of the right type and tenure.[38] Failure to support development will result in rising house prices and can constrain economic growth.

"Enabling and encouraging physical development is one of the most obvious ways that cities can help to support economic growth in their area"

Unfortunately, it is all too easy for local government to constrain growth through adverse policies. Planning is a prime example of this. Uncertainty created by the planning system can discourage business investment. In 2008, 46 percent of urban local authorities failed to decide more than 70 percent of their major planning applications within the 13 weeks suggested timeframe.[39] A clearer and faster decision making structure which recognises city-wide priorities could help improve business confidence in the planning process.

In addition to this, policy on the ground often appears to be misaligned with actual demand. This can even happen within cities. For example, in Greater Manchester there is a greater demand for more houses to be built for highly skilled workers in the affluent south of the city, rather than the north,[40] evidenced by the higher prices.

However, current planning policies seem to be restricting new housing in this area and directing it to other areas, including smaller dwellings in the conurbation's core. Excluding Manchester local authority (the conurbation core), from 2006 to 2010, 11,200 houses were built in the north of the city compared to 7,400 in the south.[41] In these instances a more strategic and coordinated approach to planning could solve this type of problem.

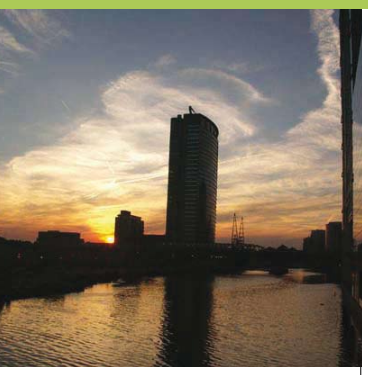
There is a particularly strong case for expanding buoyant cities. Partnerships covering buoyant cities which are seeking to generate jobs will need to ensure that their planning and housing policies allow their city to expand. For some cities, such as Cambridge, this could mean building on their greenbelt.[42] As long as this is not imposed from above, partnerships should be free to take these steps should they wish to do so.

Policy recommendations

- **Local enterprise partnerships should prepare a strategic spatial plan for their area** which reflects market demand. This would identify employment land requirements and subsequent housing need, and help plan for major investments. A spatial plan would require full buy-in from all the local authorities involved to ensure that it is implemented.

---

38. Gibbs K, O'Sullivan T & Glossop C (2008) Home Economics: How Housing Shapes City Economies, London: Centre for Cities
39. Communities and Local Government (CLG) (2009) Planning Performance Checklist - Year ending September 2008, London: CLG
40. MIER (2009) Understanding labour markets, skills and talents, Manchester: MIER
41. CLG (2010) Table 253: Housebuilding: permanent dwellings started and completed, by tenure and district, 2006/07-2009/10; In Manchester local authority 6,800 dwellings were built during this period, but there is no data for 2006/07.
42. Aldred T (2010) Arrested Development: Are we building houses in the right places? London: Centre for Cities



- To make their **planning process more business friendly**, and to encourage expansion and associated job creation, **partnerships should take on the planning decision powers for important and strategic sites.** This would include important regeneration sites, cross-boundary sites and sites with large employment potential.

- To boost the housing supply **partnerships should be free to decide whether they want or need to build on greenfield sites or on greenbelt land.**

Skills

Cities with a skilled workforce tend to perform better on a range of economic indicators.[43] The UK economy will continue to specialise in high skilled jobs and cities will need to improve their skills profile to meet the demand for these types of jobs.[44] Local enterprise partnerships should not try to over engineer the skills system, but they do have a role to play in coordinating local policy.

"Local enterprise partnerships should prepare a strategic spatial plan for their area which reflects market demand"

The Government has set out that it wants the majority of skills funding to be directed via the individual and not via government bodies or local authorities. This is likely to result in a skills policy that benefits people rather than having a focus on places.

However, a case remains for some place-based skills provision coordinated by the partnerships. For example, when there is a need to target worklessness policies at specific deprived areas a city based approach might be better. But partnerships need to think very carefully about how they customise skills provision to the local economy.[45] If they are too ambitious they may fall foul of the same overly prescriptive planning that current central government skills policy suffers from.[46]

Given patterns of mobility the case for skills policies to be tailored to a local economy need to be carefully constructed – if there is a lack of work in an area then it makes no sense to train residents up for non-existent opportunities.[47] We will look to explore this further in future work. The argument for exclusively funding high skills provision publically is also debatable, with the evidence showing that individuals capture the bulk of the benefits, through higher future earnings, and so should bear the majority of the cost.[48]

Policy recommendations

- **Local enterprise partnerships should deal with skills issues that have an immediate relevance to their economy** (e.g. a current set of firms have a specific skills need) and the interventions should focus on lower level skills (e.g. A-level equivalent and below).

---

43. Glaeser E & Saiz A (2003) 'The Rise of the Skilled City', NBER Working Papers 10191
44. Leitch Review (2006) Prosperity for all in the global economy - world class skills, London: The Stationery Office
45. For example, one of the skills requirements identified in the Leeds City Region skills strategy is 'chef skills'. While this might be a helpful opportunity area for unemployed residents, it seems less likely that this will be a constraint on the Leeds economy's growth. See Leeds City Region ESB (2010) A strategy for increasing employment and skills for the Leeds city region, LCR: Leeds.
46. Wolf A (2010) An Adult Approach to Further Education, London: IEA
47. Webber C & Swinney P (2010) Private sector cities: A new geography of opportunity, London: Centre for Cities
48. HM Treasury (UK), Federal Ministry of Finance (Germany) and Ministry of Finance (Sweden) (2008) "Social Bridges II: The Importance of Human Capital for Growth and Social Inclusion" joint policy paper, London: HM Treasury; Leitch Review (2006) Prosperity for all in the global economy - world class skills, London: The Stationery Office

- **Skills programmes delivered by partnerships in struggling cities should help residents to retrain and access opportunities wherever they might be.** A local enterprise partnership's role will be using its local knowledge to target support at specific disadvantaged groups.

Transport

A well functioning and integrated transport system is an important prerequisite for an economically successful city, reducing travel time costs for workers and businesses. Transport is one of the key drivers of the size and depth of the labour market that a place can offer to businesses, but a good transport system requires significant coordination and investment.

"A well functioning and integrated transport system is an important prerequisite for an economically successful city"

Unfortunately, our major cities' transport networks suffer from fragmented governance, under investment and poor integration. In 2008/09, the average speed travelled in Greater Manchester during the morning rush hour was just 14 miles per hour.[49] To tackle this problem, the city region is currently working to prioritise its key transport improvements through the Greater Manchester Transport Fund.[50]

While London faces severe congestion issues, in contrast to many of England's other major cities, the capital has been able to increase bus patronage and the use of public transport.[51] In part this can be explained by the level of funding that London receives and the powers that the Mayor has over transport. Central government has not yet devolved similar powers to other major cities.

Another policy innovation in London is congestion charging. As congestion charging sets a 'price' on the inconvenience imposed on other road users, it is able to tackle traffic problems in a way that the expansion of the road network or provision of public transport cannot.[52] In reality, technical difficulties remain with congestion charging, such as the initial cost of the monitoring systems, and politically it can be a hard sell. But in fiscally tight times it is an option that should not be overlooked.

Policy recommendations

- **Major cities should be looking to move towards a Transport for London style model of transport governance,** underpinned by longer term funding commitments. Cities should be able to exercise greater regulation of bus services and take control of the fare box.[53] To reduce duplication, where the geography makes sense, Integrated Transport Authorities should be incorporated into local enterprise partnerships.

- **Partnerships should take more control over strategic road and rail links to improve transport integration.** The Highways Agency and Network Rail should be required to consult with a partnership on relevant strategic road and commuter rail links.

---

49. The average person journey time per mile was 4.43 minutes, see: Department for Transport (2010) local authority congestion statistics – National Indicator 167 (variant 1)
50. AGMA (2010) Greater Manchester Local Enterprise Partnership: A proposal to government, Manchester: AGMA
51. Preston J, Marshall A & Tochtermann L (2008) On the Move: delivering integrated transport in Britain's cities, London: Centre for Cities
52. Duranton G & Turner M (2009) The Fundamental Law of Road Congestion: Evidence from US Cities, SERC discussion paper 30
53. Greater Manchester and the Leeds City Region are already taking steps towards this model. See Association of Greater Manchester Authorities (AGMA) (2009) Manchester Statutory City Region Pilot: delivering economic growth with public sector reform, Manchester: AGMA

- **Government should support any partnership attempting to introduce road user charging, for example a local congestion charge.** While political and technical implementation difficulties remain, road user charging can be an effective way of improving traffic flows. Using the partnerships to introduce a congestion charge would ensure that schemes have the backing of local businesses.

Local enterprise partnerships need a dedicated source of funding and should be incentivised to pursue economic growth

Without sufficient financial resources, local enterprise partnerships will be unable to deliver on their areas' economic priorities or help to encourage new private sector jobs. In this sub-section we argue that funding streams need to be devolved to partnerships and strong incentives put in place to encourage economic growth.

"In order to help encourage private sector jobs growth, partnerships will need new sources of funding to be devolved"

Devolving transport, skills and housing funding

In order to help encourage private sector jobs growth, partnerships will need new sources of funding to be devolved. Decentralisation without additional funding (and new finance raising powers) is unlikely to have a positive impact on local economic development. Much of the debate has focused on the future of RDA spending, but actually this is less than one percent of total government spending in the regions.[54] More important are mainstream budgets, like transport, skills and housing.

Without providing the funding partnerships need to enact their chosen policy decisions they will not really be able to operate outside of central government control. If the partnerships continue to look to central government to access all of their funding then their priorities will be shaped by the latest Whitehall policy trends rather than their economies' real needs.

The areas of funding that should be devolved include:

- a portion of the regional funding allocation for transport;
- the Bus Service Operator Grant;
- part of the Skills Funding Agency budget;
- the Homes and Communities Agency's (HCA) budget; and
- any residual RDA spend.

As an example, the Leeds City Region has recently negotiated £110 million worth of housing and regeneration funding with the HCA for 2010/11.[55] This type of settlement (although significantly smaller in future years) should be repeated and be more widespread.

Partnerships will also need to be able to use this funding as they choose – free from ringfencing. The decision on whether a transport or physical regeneration investment is most appropriate for a city's economy should be based on local priorities. Moving away from national, departmental based budgets to a local un-ringfenced pot will require a new approach to appraising projects, so that different types of intervention can be compared against each other.

---

54. Larkin K (2009) Regional Development Agencies: the facts, London: Centre for Cities
55. Homes and Communities Agency (2010) 'Leeds city region agrees £110m funding deal', press release published 13 July 2010

Rather than assessing projects solely on their contribution to departmental objectives (like traffic accidents and noise), evaluation should be based on a project's national economic contribution, ensuring that investments stimulate new activity rather than shifting it from one part of the country to another. To do this new economic appraisal tools will be required to provide a fairer basis for comparison.[56]

Some might argue that the current fiscal circumstances do not allow for further resources to be devolved. But devolution of funding does not imply increasing government expenditure, it means transferring existing central government expenditure to the local enterprise partnership level. The short term financial pressures may prevent substantial devolution of funding over the next couple of years, **but in the medium term partnerships cannot be expected to generate new private sector jobs without a more substantial source of dedicated, un-ringfenced funding.**

"The Government needs to create strong growth incentives for local enterprise partnerships"

Creating strong growth incentives

If local enterprise partnerships are given greater flexibility over their expenditure and a larger pot, then it is important that they are encouraged to pursue national macro-economic objectives. To achieve this the Government needs to create strong growth incentives for local enterprise partnerships. In the absence of incentives some partnerships may rationally choose to pursue political over economic objectives. One outcome could be that buoyant cities do not expand sufficiently, preventing enough houses from being built in their area.

The Government has already set out its Business Increase Bonus, rewarding local authorities for increasing their business rate tax base. This is a good incentive, but on its own it may be insufficient. Firstly, the bonus will only cover a six year period and secondly, it will favour the growth of property intensive businesses rather than the most productive businesses.

To supplement this incentive the Government should also reward partnerships for achieving economic growth, with a significant proportion of the funding that we have identified being allocated via a growth incentive. Two options exist for an economic growth incentive:

- **A GVA or GVA per capita based metric** – which would be a pure measure of economic performance. However, sub-regional GVA statistics would need to be improved as currently they are not timely or robust – we still only have statistics for 2007.

- **A tax income per employee based metric** – this could be an enhanced version of the Business Increase Bonus or a broader measure based on other taxes, such as income tax or corporation tax. It would face fewer practical implementation difficulties because tax information is more readily available and would still closely reflect the contribution of a city to economic growth.

56. See for example Network Rail (2010) 'Prioritising investment to support our economy: A new approach to appraisal methodology'

Local enterprise partnerships can play a role in directly supporting business growth, though the approach needs to be more realistic

While partnerships should focus on improving the general business environment and getting the basics right, a justification remains for continuing to have an active business policy at the sub-national level. History shows that the public sector has often been involved in industrial upgrading and that significant market failures do exist, particularly in new areas of economic activity.[57]

However, even proponents of an extensive industrial policy would recognise that the lack of money means that the scope for intervention over the next five years will be limited, and a very different approach from that undertaken by the RDAs will be required. Resource constraints means that partnerships will need to prioritise their actions and the objectives of industrial policy will need to be more realistic.

This sub-section suggests the role for local enterprise partnerships in utilising business engagement, supporting high growth firms and responding to supply side shocks.

"Engaging with local businesses of all sizes will allow the partnerships to access new knowledge and to get a better understanding of their private sector economy"

Utilising business engagement

Business engagement will be fundamental to the success of the partnerships. Stronger business links should lead to policy that better meets businesses' growth needs. Engaging with local businesses of all sizes will allow the partnerships to access new knowledge and to get a better understanding of their private sector economy.

While some cities already achieve a high level of engagement with the private sector others have been less successful.[58] For example, a recent study found that 59 percent of local authority websites are rated as poor and 19 percent had no relevant information with regard to providing businesses with the information they need to deal with government, such as the formal paperwork required for setting up a company.[59]

Policy recommendations

- **Business engagement should be used to design and direct the interventions that partnerships make.** Asking firms what they need to expand and create new jobs should be the way that partnerships decide on what interventions to make to directly support business growth. In order to ensure that preference is not given to particular business interests, the process of engagement, and its policy outcomes, needs to be accountable and transparent.

---

57. Lin J Y & Monga C (2010) Growth Identification and Facilitation: the role of the state in the dynamics of structural change, World Bank Working Paper 5513; Hausmann R & Rodrik D (2006) Doomed to Choose: industrial policy as a predicament, paper presented at Centre for International Development, Harvard University, 9 September 2006
58. Tucker M & Neat S (2008) Raising the Bar: driving local authority and private sector engagement, Leicester: CFE
59. Socitm (2010) Better connected for business: implementation of the EU Services Directive in the UK in 2010, Northampton: Socitm

- **Partnerships should address coordination failures.**[60] These occur when a desired outcome does not take place because it requires a number of simultaneous actions (such as multiple investments) by a range of firms.[61] In these instances a partnership has a role to play in coordinating (but not funding) the businesses it works with. One example would be a local enterprise partnership organising the provision of a particular type of specialist training, required by a number of local firms, but currently not being provided. Creative Sheffield is currently undertaking a coordination role like this for manufacturing firms in the city.

Policies to support high growth firms

As explained in section one, there is a case for partnerships to focus more of their attention on supporting high growth firms because they are responsible for a large share of a city's employment growth. While there are some obvious things that the partnerships can do to support high growth firms there are also some potential pitfalls with this type of support.

"The most important assistance that a partnership can provide is to take simple steps to ensure that local firms that want to grow are able to grow"

The most important assistance that a partnership can provide is to take simple steps to ensure that local firms that want to grow are able to grow. This could include assisting firms that want to expand their premises to gain planning permission. If the business environment in a city does not fit the needs of local businesses, mobile firms will leave and others will underperform.

In terms of business support, focusing on high growth firms in part implies providing better quality support to fewer businesses, at a reduced overall cost. Evaluations have suggested that more intensive support provided to fewer firms, perhaps seven to ten percent of the existing recipients, will probably provide better value for money than a scattergun approach.[62] However, partnerships need to be cautious as the effectiveness of government funded business support is hotly contested. It is not always clear that the benefits derived are worth the cost and some of the market failure justifications have probably been overemphasised.[63]

Rather than trying to 'pick out' high growth firms, partnerships need to try to channel support toward **potential high growth firms**, where there is a rationale for public intervention to do so.[64] This could be done by requiring supported firms to demonstrate their growth plans and for payment to be

---

60. Rodrik D (2004) Industrial Policy for the Twenty-First Century, CEPR Discussion Papers 4767
61. Coordination failures happen when a certain desirable activity fails to take place because private actors fail to coordinate their plans. This is because each firm's decision is based on a set of incentives but without knowledge of the the decisions of other firms. At the same time each firm's decision influences the set of outcomes available to other firms. In these circumstances a sub-optimal outcome may result. Coordination failures are a type of market failure, where if the firms were to coordinate to all take a set of actions welfare would be increased.
62. Mole K, Hart M, Roper S& Saal D (2009) Broader of Deeper? Exploring the most effective intervention profile for public small business support, Working Paper No. 105, Warwick: Warwick Business School
63. Bennett R (2008) 'SME policy support in Britain since the 1990s: what have we learnt?, Environment and Planning C: Government and Policy Vol 26: 375-397
64. Alongside the standard justifications for business support, there are two other market failures that could warrant supporting high growth firms. Firstly, it has been demonstrated that there is no real link between firm productivity and growth; if this is the case it means the market is not working as effectively as it could by selecting the best firms. As such there could be a reason for the government to support the growth of productive firms (see Coad A (2007) 'Firm Growth: A survey', Papers on Economics and Evolution 2007-03, Max Planck Institute of Economics). Secondly, firms that operate in new markets produce information about the potential for profits in those markets that can be freely used by other firms. The information created is an externality, thus there is a reasonable role for government to intervene and try and correct for this (see Hausmann R & Rodrik D (2003) 'Economic development as self-discovery', Journal of Development Economics Vol 72(2): 603-633).

linked to employment or turnover growth. The type of consultancy offered should be based around improving productivity[65] and 'soft support', such as aiding management changes that facilitate expansion.

It also important that public policy only intervenes where there is a good reason to do so. Most high growth firms are succeeding without any intervention and as such there is no reason for partnerships to suddenly become involved.

Policy recommendations

- **Local enterprise partnerships need to engage with high growth firms to understand their business needs.** Firms themselves will be able to give the partnerships the clearest idea of the policies that would support their expansion, if any. The firms that partnerships engage with will need to be continually refreshed to ensure that the partnerships are meeting the needs of local high growth firms, which are unlikely to be involved in existing networks.

- **Partnerships need to act responsively towards the expansion plans of high growth firms.** This means supporting firms that have plans to expand by swiftly granting them planning permission for site development.

- **Partnerships should consider commissioning small teams of highly qualified business analysts rather than providing generic business support.** These advisers would have more business experience than current business support staff and would also be paid more, with a significant element of performance-related pay.[66]

"Partnerships need to act responsively towards the expansion plans of high growth firms"

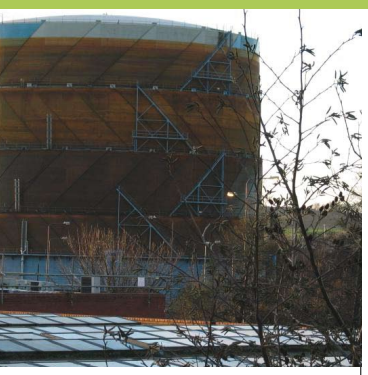
Preparing for supply side shocks

The loss of a large employer or the decline of an industry in a city can have a big impact on a local economy. Those made redundant tend to find they do not have the right skills to find employment in another industry, while vacancies in their own industry are scarce.

Previously, industrial policy often attempted to prevent plant closures, but this approach was unsuccessful and usually only postponed the negative impact. It is time to move away from resisting change towards easing transition. Local enterprise partnerships should play a role in supporting vulnerable people affected by changing economic circumstances.

---

65. Particularly total factor productivity, not related to the increase in labour and capital inputs.
66. Structuring the analysts' contracts will be very important to the overall success of the policy. We suggest that the partnerships would pay a proportion of the advisers' salary, with the advisers also receiving money from the firms they provide consultancy to. In effect, the partnerships provide part-subsidised high quality support to a small number of firms. A large proportion of the analysts' salary should be based on performance based bonuses for helping firms to achieve high growth (with the cost split between the partnership and firm). This would ensure that the advisers themselves are incentivised to identify potential high growth firms.



Box 2: The five key lessons for dealing with supply side shocks are:

1. to **bring together public sector agencies in a location** to work together on dealing with the impact of a plant closure;
2. to **advise workers on employment opportunities,** legal rights, the take up of benefits and how to deal with debt;
3. to make specific **health based interventions that build up the psychological resources of the underemployed and unemployed** ex-workers to improve well being;
4. to **extend and adapt mainstream training provision** to help workers to find suitable courses, providing short flexible training that workers can access while they are still in work; and
5. to provide additional funding **to allow new employers to send workers affected by a closure on training courses** and to **pay for affected workers' travel to training courses and job interviews.**

"Partnerships should put procedures in place to deal with shocks if and when they arise"

As major supply side shocks are a rare occurrence, the funding for these types of intervention should be held nationally. However, local enterprise partnerships are well placed to plan and coordinate action.

Policy recommendations

- **Partnerships should put procedures in place to deal with shocks if and when they arise**, particularly in cities that are heavily dependent on one company or industry and in those places set to be hit by public sector job losses. Partnerships need to retain the capacity and institutional memory of RDAs to deal with large scale plant closures.

- **Partnerships should learn from previous examples of the management of supply side shocks.** Two high profile plant closures in recent years have been the MG Rover car plant in Longbridge in 2005 and the part-mothballing of production at the Corus steel plant in Teesside in February 2010. They provide a good guide for local action.[67]

67. For a comprehensive evaluation of the policies put in to place in response to the Longbridge closure see: Bailey D, Chapain C, Mahdon M & Fauth R (2008) Life after Longbridge: Three Years on. Pathways to re-employment in a restructuring economy, London: The Work Foundation

3. How can national policy support private sector jobs growth in cities?

Local enterprise partnerships will be able to access some funding through the Regional Growth Fund, which was announced by George Osborne in his Budget speech. The fund will allocate £500 million each year for the years 2011/12 and 2012/13 towards local economic development.

The Regional Growth Fund will be used to support the Government's ambition to rebalance economic growth across the country. Two key objectives for the fund have emerged. The first is that it should support private sector enterprise by targeting projects with significant potential to generate private sector jobs and stimulate economic growth. The second is that it should stimulate private sector jobs growth in places that will be hit hardest by public sector job cuts.

"The Government is at risk of conflating the objectives of the fund"

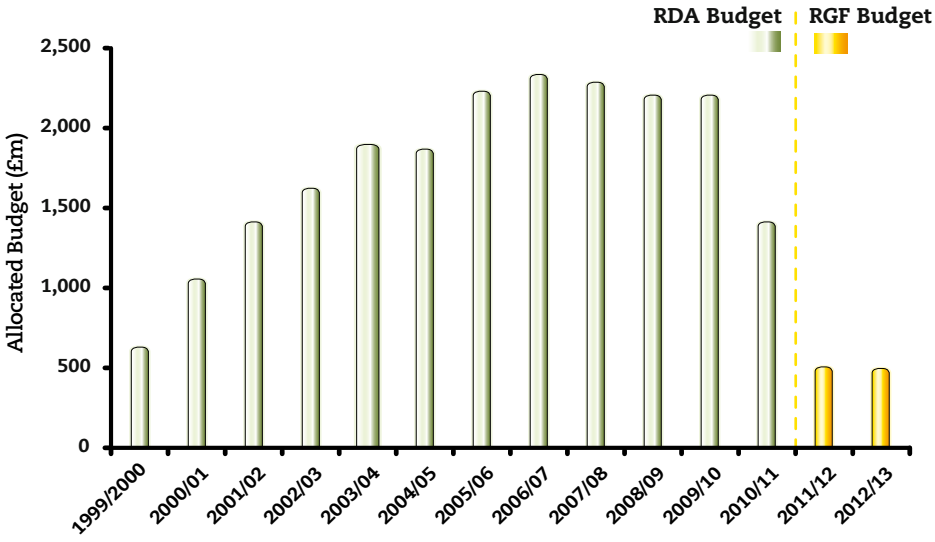
The Government is at risk of conflating the objectives of the fund. This section suggests what we believe the objectives of the Regional Growth Fund should be. It makes three main points:

- **The Regional Growth Fund is small in comparison to the budgets of RDAs.** Expectations of what the fund will be able to do should be matched to this reality.
- **The objectives of the fund need clarification.** It should not prioritise creating private sector jobs in public sector dependent cities. Instead it should have two independent objectives:
  - **Stimulate private sector jobs growth in more buoyant economies**, such as Reading and Bristol, where private sector jobs growth is most likely to be sustained; and
  - **Manage transition in struggling cities**, such as Middlesbrough and Blackburn, that will need support in dealing with issues resulting from economic decline.
- Funding should be split between these two objectives so that the **main emphasis of the fund remains on supporting private sector jobs growth.**

The Regional Growth Fund is small

Both national and local government need to be realistic about what can be achieved by the Regional Growth Fund. The fund is only one third of the size of the RDA budget for 2010/11, and it is less than one quarter of the £2.2 billion RDAs had to spend in 2009/10. Looking over the longer term, in total the RDAs will have been allocated £21.1 billion since 1999/2000 by the end of 2010/11 (see Figure 9).

Figure 9: Allocated RDA and Regional Growth Fund annual budgets



Source: *Taxpayers' Alliance (2008) Structure of Government No.3: The Case for Abolishing Regional Development Agencies; BIS (2007) RDA Finance & Governance; HM Government (2010) Consultation on the Regional Growth Fund*

"The fund needs to be focused on those areas and types of investment that can deliver maximum private sector jobs growth"

To put this in perspective, £364 million of public money was spent on the regeneration of Liverpool city centre between 1999 and 2008.[68] And £711 million was spent on infrastructure in Newcastle between 2002/03 and 2006/07.[69]

It is also important to consider the time frames on these projects. Regional Growth Fund spending will not create permanent jobs overnight. It often takes many years for projects to be completed and for their full benefits to be realised.

Due to these reasons, the number of projects that the fund will be able to support relative to the activities of the RDAs will be limited.

In times of fiscal constraint money must go where it will have maximum impact

Given the size of the Regional Growth Fund, this limited pot of funding should be spent where it will support the most job creation. In order to do this, the fund needs to be focused on those areas and types of investment that can deliver maximum private sector jobs growth. And sustainable job creation is more likely to occur in more buoyant economies, such as Brighton and Milton Keynes.

The Government currently wants to use the fund in part to stimulate jobs growth in areas that are over reliant on the public sector. The problem with this is that many areas that are vulnerable to public sector job cuts have weak private sector economies. Trying to stimulate private sector jobs growth in Barnsley, a city that lost 3,500 net private sector jobs between 1998 and 2008 and has one third of its jobs in the public sector, is unlikely to result in sustainable private sector job creation.

---

68. Liverpool Vision (2008) Make no Little Plans. The Regeneration of Liverpool City Centre 1999-2008. Although not all of this money came from regional development agencies (NWDA contributed just over £100m in Liverpool), these examples give an illustration of the cost of such schemes at a time when all public spending on economic development will be squeezed.
69. Newcastle City Council (2008) Strategic Capital and Asset Management Plan

More generally, if the Government is trying to maximise private sector jobs growth then it is important to recognise that the evidence suggests that sustainable private sector job creation is more likely to occur in stronger economies such as Leeds than it is in struggling economies such as Hull.[70] Struggling cities already suffer from weak demand for labour. Subsidising further expansion in areas of weak demand, for example through the building of office space, is a poor use of limited public money. This will only compound existing property oversupply issues which these cities are already faced with.

This is not to say that places which struggle to create private sector jobs should not be given any help by government. These cities need intensive government support to help them deal with public sector job losses that will have a large impact on their economy. However, policy makers should not confuse the objective of rebalancing and private sector jobs growth with the goal of helping cities to deal with public sector job losses because these two policies are not necessarily complementary.

"Policy makers should not confuse the objective of rebalancing and private sector jobs growth with the goal of helping cities to deal with public sector job losses"

The objectives of the growth fund

Based on the evidence, the Regional Growth Fund should have two independent objectives, to:

(a) **Stimulate private sector jobs growth;**

(b) **Help struggling cities hit hard by public and private sector job losses.**

(a) Stimulate private sector job growth

Bids under this objective should be approved only if they will support sustainable private sector jobs growth

England needs to generate private sector employment growth to replace the jobs lost as a result of the recession and offset the coming job losses due the cuts to the public sector. So quite rightly, a key focus of current Government policy is to support private sector jobs growth. Given the limited amount of funding available this objective should be focused in areas of high private sector demand.

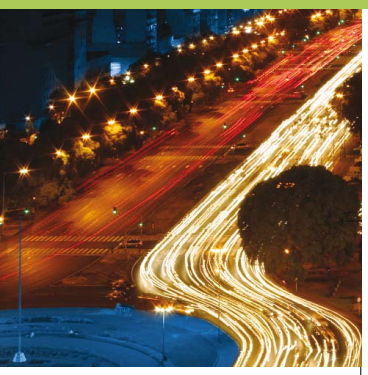
Bids should focus on capital projects where there is a market failure

Spending should focus on supply side projects that are likely to deliver wider benefits to local economies and support job creation, such as key transport links and infrastructure, land remediation and physical regeneration projects. In reality, a handful of these projects is likely to take up the majority of the fund.

Investment is important for long term economic growth.[71] So given its small size, the Regional Growth Fund should also have a greater focus on capital projects that are likely to generate significant long term economic returns rather than being spread thinly over many small scale policy initiatives. This is because policy initiatives, such as attempts to boost enterprise in deprived areas, appear to have had little impact.[72]

---

70. Webber C & Swinney P (2010) Private Sector Cities: A New Geography of Opportunity, London: Centre for Cities
71. Romer P (1990) Endogenous Technological Change, Journal of Political Economy Vol 98 (5) Oct. 1990
72. Swinney P (2010) UK cities: Do they mean business? London; Centre for Cities



Size should not preclude the type of bid that receives funding – for example, reducing congestion at a junction may deliver large benefits to a local economy for a small outlay.[73] However, if the fund attempts to support too many projects, political considerations may lead to less effective projects receiving funding.

Bids should be backed by the private sector where feasible

Often policies of the past, such as those of RDAs, have attempted to stimulate economic activity in cities with low demand rather than working in areas where private sector demand is already strong. Unfortunately, these attempts to boost demand failed to adequately stimulate private sector job creation.[74]

The Government has stated that it will favour bids to the Regional Growth Fund that can demonstrate that they have financial backing from the private sector. This is important for two reasons. Firstly, it will allow the Government to leverage as much money as possible from its own investment. Secondly, it will act as a guide as to where private sector demand is highest and signal the economic viability of a project. Private sector leverage is not a perfect measure of where job creation will be the most sustainable, but it is likely to be a more reliable guide than job creation projections.[75]

"Private sector leverage is not a perfect measure of where job creation will be the most sustainable, but it is likely to be a more reliable guide than job creation projections"

Case Study – Temple Quay 1, Bristol

The Temple Quay 1 development in Bristol is a good example of the type of project that should be eligible for money from the Regional Growth Fund. Temple Quay was a regeneration project in Bristol city centre, mainly creating grade A office space. Public money was used to bring together fragmented land and to remove contamination in the area. This then allowed private sector investment to proceed on the site.

The land preparation cost the public purse £21.25m.[76] But this leveraged around £260m of private sector investment, and it created 820 net new jobs in the city.[77]

Although the scale of the leverage of this project is somewhat of a rarity, and it took several years to complete, it provides a good example of the types of bids that should be supported under the first objective of the fund.

However, the private sector is unlikely to back all projects that will bring benefit to a city economy, such as transport projects to ease congestion. This is not because they are not viable, but because specific private sector actors will not be able to make a return on this investment. However, transport bids backed by a Business Rate Supplement, which is supported by business, should be looked upon favourably, as this indicates clear demand from the private sector of a project's importance.

When private sector leverage does not provide guidance, the Independent Approval Panel, which will assess which bids will be given funding, should be guided by appraisals of bids undertaken using Green Book methodology to demonstrate the economic rationale for public sector intervention.

---

73. Eddington R (2006) The Eddington Transport Study, London: Department for Transport
74. Webber C & Swinney P (2010) Private Sector Cities: A New Geography of Opportunity, London: Centre for Cities
75. Bidders want money, and so they are incentivised to exaggerate the outcomes of a project, such as job projections, to make their bid look more attractive. As such, these projections should be treated with caution.
76. After receipts of £11.6m, net public investment was £9.7m.
77. South West Regional Development Agency (2006) Evaluation of Public Sector Involvement in Temple Quay 1

Green Book methodology will not be able to offer full guidance on which bids to select. While it offers a consistent broad approach to analysis, it has historically been applied differently by different government departments and does not provide the consistent practical tools that will be necessary to assess the implications of schemes for economic growth. The Independent Approval Panel will need to consider further ways of comparing the benefits of different types of investments alongside private sector leverage.

(b) Help manage transition

Struggling places should not be ignored

We do not think that cities which are unable to deliver sustainable private sector growth should be ignored by government. They have issues that need to be addressed by public funding, and the economic activity that does occur in these cities should be supported. Although currently struggling, this isn't to say that these places will not grow again in the future. But previous policies have created barriers to economic adjustment that ultimately harm rather than help the economies of struggling cities and the people who live in them. These cities need funding to support adjustment in their economies before sustainable private sector jobs growth can occur.

"Previous policies have created barriers to economic adjustment that ultimately harm rather than help the economies of struggling cities"

Bids should look to improve the quality of the built environment

Economic decline impacts upon both the built environment of a city and the people who live in it. Net out-migration creates pockets of residential abandonment, while decaying industrial infrastructure contributes to urban blight. This creates an impact beyond the cost related to the inactive use of a site and as a result these costs have the potential to spiral.

These problems negatively affect the quality of life of people who live in cities struggling with economic change, so these cities should also be given funding to invest in, or demolish, these buildings according to the needs of the community. This means moving away from viewing dereliction simply as a redevelopment opportunity, especially when this results in an oversupply of housing or commercial space. Public investment should continue in the public realm if it is likely to benefit the existing business base and the quality of life of residents in a city. The third paper in the Agenda for Growth research series, which will be published in November, will focus in more detail on struggling cities and the built environment.

Bids should have a greater focus on the outcomes for people

Although demolition of derelict buildings and improvement of the public realm should improve the quality of life of residents, it is unlikely to improve their economic outcomes. So whereas in the past regeneration policy has been heavily weighted towards the built environment, a better approach would be for policymakers to have a greater focus on the outcomes for people.

Struggling cities tend to have poorer skills profiles than more buoyant ones, as shown in Figure 10. Whereas less than one in ten people have no formal qualifications in Reading, almost one in six have no formal training in Bolton.[78]

---

78. NOMIS (2010) Annual Population Survey, 2009 data

So the Regional Growth Fund should aim to invest in targeted skills programmes to improve skill levels in these cities. For example, Bolton should aim to retrain its pool of unskilled labour, particularly in the 16-24 age group – 16 percent of 16-24 year olds have no qualifications. However, policy makers should note that it is unlikely that all beneficiaries of such programmes will apply their new skills in the city economy. Some people will seek out greater opportunity elsewhere.

"Funding should be weighted towards supporting private sector job creation"

Figure 10: Percentage of working age residents with no formal qualifications (2009)

Buoyant cities	Percentage of working age residents with no formal qualifications	Struggling cities	Percentage of working age residents with no formal qualifications
Cambridge	5.3	Birkenhead	12.3
Brighton	7.3	Burnley	13.0
Aldershot	7.6	Barnsley	15.3
Reading	7.7	Bolton	15.8
Oxford	8.5	Middlesbrough	15.9
Bristol	9.1	Stoke	16.5
Milton Keynes	9.3	Blackburn	18.2
London	11.4	Hull	18.2
Crawley	12.7		

Source: *NOMIS 2010, Annual Population Survey (Jan-Dec 2009 data)*

Bids should be backed by other public sector funding

The fund is unlikely to be able to leverage private sector investment for bids aiming to manage transition because these investments will struggle to generate a commercial return. So as with projects in the first objective that do not provide a commercial return, bids submitted under this objective must demonstrate that they address a market failure, can be delivered at reasonable cost and should be assessed using Green Book methodology.

Funding granted to help manage transition should be matched with other public sector funding streams where possible. Despite severe public funding constraints, the Regional Growth Fund is not the only funding for cities. Any money received from the fund should be coordinated with projects funded from other sources in order to achieve a more coordinated approach to economic development. Two examples of such a source are existing local authority budgets and the European Regional Development Fund.

Funding should be weighted towards supporting private sector job creation

The Government has proposed that the fund aims to stimulate private sector jobs growth. And although we have proposed two differing objectives, we think that the main emphasis should remain strongly on trying to stimulate growth. This should be reflected in the allocation of funding between the two objectives, which should heavily favour the first objective.

Conclusion

Major public spending constraints and an uncertain economic environment mean that national and local government face an uphill struggle in achieving their objectives around economic growth. Policy approaches towards sub-national growth need to be more realistic and they need to deploy scarce public sector resources more effectively than they have in the past. This paper has provided decision makers at all levels of government with some advice about how this can be achieved.

The paper's key recommendations can be summarised as follows:

"Attitudes towards economic rebalancing and business growth policy need to be more realistic across all levels of government"

- **Attitudes towards economic rebalancing and business growth policy need to be more realistic across all levels of government.**
  As shown here, and in more detail in our recent *Private Sector Cities* report, a significant spatial rebalancing of the economy is not an achievable goal, even during an economic boom. Nor will a successful manufacturing renaissance provide the kind of jobs boost that England's economy needs. And not every city can have a creative industries or life sciences cluster to generate future private sector jobs.

  Government does have a role to play in supporting business growth, but it needs to be more practical about how it approaches this challenge and focus resources where they can have maximum impact. This could mean paying more attention to high growth firms.

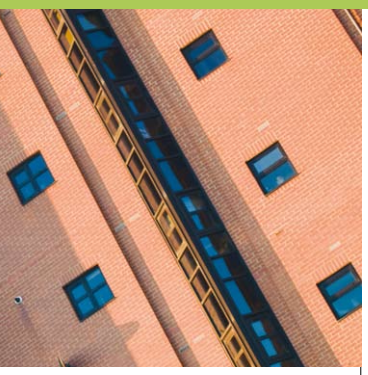
- **Local enterprise partnerships should be given their own un-ringfenced source of funding and should focus on getting the basics right in their areas by improving skills and the general business environment.**
  This means focusing on improving transport, housing and other infrastructure provision, as well as improving lower level workforce skills. Partnerships should also concentrate on working together to pool resources and coordinate policies – particularly around planning and transport.

- **The Regional Growth Fund should primarily be used to support jobs growth in areas where job creation can be sustained.**
  Expectations about what can be achieved with the fund should be managed because the size of the funding pot – £1 billion over two years – is small compared to previous spending in this area. When deciding how to spend the money, the emphasis should be on maximising private sector growth in those areas where it can be sustained and supporting transition in those areas struggling with the legacy of long term industrial change. The emphasis on attempting to stimulate sustainable jobs growth in areas more vulnerable to public sector job cuts should be dropped.

Definitions

This report contains statistical data from ONS which is Crown copyright and reproduced with the permission of the controller of HMSO and Queen's Printer for Scotland. The use of the ONS statistical data in this work does not imply the endorsement of the ONS in relation to the interpretation or analysis of the statistical data. The analysis upon which this report is based uses research datasets which may not exactly reproduce National Statistics aggregates.

The Centre for Cities uses Primary Urban Areas (PUAs) to define the 56 England cities in this report. These PUAs were defined by the Department for Communities and Local Government in their 2005 State of the Cities Report. The definitions of PUAs can be found here: www.centreforcities.org/pua



Agenda for Growth

The Centre for Cities' *Agenda for Growth* research programme will set out a radical new approach to economic growth in England's cities. Our aim is to provide high quality analysis and advice that helps cities and national government think about how they can work together to raise economic growth and generate more private sector jobs.

We will be publishing three major reports as part of this series in 2010. They will analyse the challenges of economic growth in England's cities and set out what we see as the key components of a more realistic, evidence-based approach.

Private sector cities: Our first paper analysed variations in private sector jobs growth across England and provided a new typology of change in England's cities. It showed that there has been a major shift in the potential for private sector jobs growth across the country and argued that policy makers at the local and national levels need to respond by adjusting their strategies for different types of cities.

Firm Intentions: This second paper explains some key lessons on the nature of private sector growth in England and explores the policies that can be used to support private sector jobs growth as the public sector begins to contract. In particular, we look at how local enterprise partnerships and the Regional Growth Fund can be used to help stimulate jobs growth in cities across the country.

Renewing struggling cities: The third paper will set out a new strategy for physical regeneration in underperforming cities. We will explain why the objectives of built environment policies in cities that have been struggling with persistent poor performance need to change and set out the content of a new strategy.

If you would like to discuss, comment on or sponsor future work in this series please contact **Chris Webber** on 020 7803 4314 / **c.webber@centreforcities.org**

With support from

City partners

September 2010

Enterprise House
59 - 65 Upper Ground
London SE1 9PQ

t **020 7803 4300**
www.centreforcities.org